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The Housing Market and Retirement Planning

Across the entire country, home values have dropped in the last few years — in some areas significantly. The news isn't all bad though:

- The impact is regional — some markets are much less affected than others.
- Some of the worst markets appear to have bottomed.

- Great homes in great neighborhoods are still in demand.
- New housing starts have been at a record low, which is good for existing home sales.
- In many areas, higher-end homes are not as hard hit as moderate to low-end homes.

"Yesterday is a cancelled check. Tomorrow is a promissory note. Today is the only cash you have — spend it wisely." ~ Kay Lyons

The news has been dominated by negative financial reports on issues over which you have no control. It is important to be an informed financial consumer but be cautious and deliberate about media consumption. Financial stress can undermine your sense of well-being.

Worrying doesn't change a thing, but it can steal precious hours from your day. Take steps to manage the financial stressors in your life. Focus attention on areas where you can positively impact your financial situation.

- Establish/review financial goals and long-term financial strategy.
- Meet with your advisor to review risk tolerance and investment allocations.
- Monitor spending and take steps to improve your savings and cash flow.
- Calculate and track net worth — a benchmark for monitoring your progress.
- Review your beneficiary designations and estate plan.

These are just a few suggestions to consider. Your situation is unique. It is important to take the time to identify specific needs and to formulate a plan of action. Be proactive.

In the meantime, set aside time to have fun doing whatever you enjoy most. Today will soon be a cancelled check — spend it wisely!

Charlene K. Dolan

And finally, activity will not stop — people will move, buy, and sell. Homes are in fact selling now, and that activity will continue to pick up as unemployment decreases and the economy recovers.

According to the Case/Shiller Index, which tracks U.S. housing values, home prices have traditionally followed a slow but steady incline. The upward spike we experienced from 2005 to 2007 was quite the anomaly and not one we're likely to see again in the baby boomer lifespan.

This may impact you in several ways. Perhaps your home no longer provides as great a backup retirement income plan as you may have anticipated or will provide a smaller inheritance for your children. Or perhaps you've considered relocating to a senior community but have delayed that move to wait and sell your home when prices recover.

However, it's not likely we'll return to the overvalued housing bubble of 2006. Even though it feels like we've experienced this tremendous drop in value, consider what your home was worth back around 2003–2004. At the national level, we've not only returned to those levels but are in fact near where they would be had prices simply continued their slow, steady climb without the spike.

If you can erase from your mind the potential gains had you sold your house in 2006, chances are that your home has still proven to be a sound long-term investment.

Future Homebuyers

According to the 2010 Urban Land Institute Report entitled, *Housing in America*:

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Housing Market

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The Next Decade, going forward, the rate of house appreciation is likely to revert closer to the long-term norms (pre-2006) of 0.75% to 1% per year over the rate of inflation — not double-digit annual increases.

As the national unemployment rate remains high, the rate of home ownership will drop — since buying a home limits the ability to move to areas with jobs.

The report estimates that 15% of homes with mortgages will be foreclosed by the end of 2010. Also, as many as 15 million Americans now have impaired credit scores that will limit their ability to purchase a home for the next 10 years.

As far as staying in a home until housing prices increase, consider the potential homebuyer of the future —and whether your house will appeal to this market.

Generation Y is young in their careers and highly impacted by job instability, flat or declining incomes, and tightened credit, so it is more apt to rent longer than the baby boomers.

Generation X has learned difficult economic lessons while nearing mid-career. These 30+ folks are less apt to “trade up” from modest housing, choosing instead to save and invest their money.

The flood of future immigrants, expected to save the labor shortage caused by retiring baby boomers, are less likely to command high salaries and buy upscale homes.

Baby boomers will spend the next couple of decades recouping income and investment losses suffered in recent years and be less inclined to “trade up” to more expensive homes.

Current Investment Advice

In the news recently, financial experts have cautioned homeowners and homebuyers that a house should no longer be considered a high-performing asset, but rather a place to enjoy living over a long period of time. There are a couple of reasons for this.

First of all, economists want to promote consumerism — encourage people to continue buying homes. No one wants to hear that real estate prices will continue to fall or stay flat or that there won't be enough people in future generations to buy all the houses baby boomers will vacate when they downsize, move to senior communities, or simply pass away.

Second, they also want consumers to seek out other investment vehicles rather than pour money into an expensive home

with an exorbitant mortgage. This will serve to flow more money into capital markets to help fund public companies, thus improving the unemployment rate.

In today's environment, taking on a modest mortgage and paying it off before retirement is the goal. At that time, and based on individual situations, you will have the option to downsize your residence and use the equity to help fund your retirement. Or, stay in the home until you pass away and let your home's value serve as an inheritance.

A Harder Working Asset

The question in today's homeowner market isn't how much the value of your home has dropped, but rather will your house sell? Well-built homes in highly sought-after neighborhoods can sell for a fair price in today's market. People with the

means to qualify for a mortgage are interested in trading up to the community they want to be in *at a fair price* — as opposed to an inflated one. If you put a house on today's market at or near its 2006-inflated rate, it's not likely to sell.

And for an empty-nester/pre-retiree who would do well to downsize, you can most certainly scoop up a smaller, quality home suitable for your needs while home prices and interest rates are low.

The only question left for you is can you secure a strong, long-term rate of return or a guaranteed source of retirement income if you downsize and receive an influx of cash? Please call so we can discuss how today's home values can lead to tomorrow's retirement income opportunities. ○○○

Coping with the College Debt Crisis

America reached an ominous milestone last year. For the first time in history, U.S. student college debt exceeded credit card debt. According to the Project on Student Debt, college and graduate students are adding education debt at the rate of \$2,853.88 per second, which means they will reach the \$1 trillion mark sometime next year.

Thousands of graduates are saddled with debt they can't afford to pay. Student default rates have doubled since 2005, according to the U.S. Department of Education.

To more sharply define the issue, in 2009, the average college student graduated with an education loan debt of \$24,000, up 6% over the prior year. Debt loads for graduates of private colleges are higher, and it's not unusual for college graduates to leave school with more than \$100,000 in debt and monthly payments of \$700 or more. For many recent graduates, the weak economy means they are either unemployed or underemployed and unable to keep up with even minimal payments.

For graduates with large amounts of private loan debt, there is little they can do — the law makes it extremely difficult to discharge educational debt via bankruptcy. Debt consolidation — one avenue previ-

ously open — has been severely limited by the decrease in the number of banks willing to extend private loans. At best, holders of private loans can ask to lengthen the terms of their loans, but many lenders are reluctant to make even this concession.

Holders of federally guaranteed loans have more latitude. Since July 1, 2009, graduates have been eligible to apply for the Income-Based Repayment Plan. Under the terms of this program, the federal government agrees to limit annual repayment to no more than 10% of a graduate's income. Single people with less than \$50,000 of income and married couples with two children and less than \$100,000 in joint income are eligible.

Meanwhile, federal loan programs offer graduates other forms of relief, including a graduated repayment program, extended repayment terms of up to 25 or 30 years, and the option to have payments suspended because of financial hardship.

The best form of relief, however, is prevention. Parents should caution their students against taking out large loans, especially private loans. Before deciding whether to enroll in a college or university, it would serve parents and students well to project how much they might need to meet the bills. ○○○

Roth IRAs: Are They for You?

Unlike a traditional individual retirement account (IRA), contributions to a Roth IRA are taxed while the earnings accumulate tax free. What's more, a Roth IRA can be funded with new money or converted from a traditional IRA. But is it for you?

Are you worried about an increase in tax rates? Many experts are concerned that rising deficits will force Congress to raise taxes. By investing in a Roth IRA before any potential tax increases, you can take advantage of current tax rates. This beats the traditional IRA where you would be paying taxes at a higher rate when you make a withdrawal in the future, except...

...that most people fall into a lower tax bracket when they retire. Also consider this: if you convert your assets into a Roth IRA, it could take 15 to 20 years for the tax-free growth of a Roth IRA to make up for the taxes paid at the time of conversion. Or even longer if you make regular withdrawals from the account.

In other words, depending on your age, how close you are to retirement, and your pre- and post-retirement income levels, the tax benefits of a Roth IRAs may or may not make sense for you.

How do the new rules affect you? One of the reasons Roth IRAs have become more attractive recently is because of their new income restrictions — or lack thereof. In the past, anyone making more than \$100,000 a year couldn't convert their traditional IRA into a Roth. Starting in 2010, they can.

The law hasn't, however, impacted annual contribution limits. The maximum annual contribution allowed for a Roth IRA remains \$5,000 for anyone under 50 years old and \$6,000 for investors 50 or older.

Does passing on wealth matter to you? A benefit of Roth IRAs is that you can pass the balance on to your beneficiaries tax free. Additionally,

there are no minimum withdrawals required for a Roth IRA — you can take advantage of tax-free growth for as long as you like.

Consider this example: a grandmother passed away shortly after converting \$30,000 to a Roth IRA. She named her six-year-old granddaughter as her beneficiary. The granddaughter begins withdrawing the minimum amount each year. Assuming the investments in the grandmother's Roth IRA earn 8% per year and the granddaughter continues withdrawing just the minimum amount required each year by law (IRS rules give a six-year-old 75 years to empty an inherited IRA), the granddaughter will receive \$2.1 million from the \$30,000 her grandmother converted to the Roth IRA. And

every cent will be income-tax free (Source: Fox Business, 2010). *(This example was provided for illustrative purposes only and is not intended to project the performance of a specific investment vehicle.)*

Roth IRAs clearly offer a number of attractive benefits when compared to traditional IRAs. But those benefits are a tradeoff: pay taxes now or pay them when you're retired. Consider whether the benefits of a Roth IRA — including the comfort of paying taxes today at a known rate — really matter to you.

Because everyone's situation is different, you should take the time to carefully review whether a Roth IRA is for you. Please call if you need help. ○○○

Separating Your Risk

Your willingness to assume risk with your investments is not necessarily a static concept. You may be less willing to take risk with investments designated for an essential financial goal, while you may be more willing to take risk for nonessential goals. However, those varying risk levels may be difficult to assess if all your investments are commingled in one account.

For instance, assume you have three goals — to ensure you have enough funds to support yourself through retirement, to send your children to Ivy-league colleges, and to purchase a vacation home. The most crucial goal is to ensure you don't run out of money during retirement. Thus, you want a high level of assurance that you'll reach that goal, devoting a substantial portion of your resources to the pursuit of it. Your investments for that goal are likely to be somewhat conservative, especially as you approach retirement age. The next important goal is sending your children to Ivy-league colleges. You have more limited resources to

devote to that goal, plus your children can attend less-expensive colleges or pay part of the costs themselves. For that goal, you may be willing to assume more risk with your investments to increase the likelihood of reaching that goal. Your goal for a vacation home is clearly last, so you may have few resources to devote to it. For that goal, you may be willing to use very aggressive investments, since that may be the only way you can achieve that goal.

The point is that your willingness to assume risk is not static. It will vary depending on how important the goal is to you and how much you can designate to that goal. Commingling all your investments for all goals in one account may make it difficult to analyze your investments in this manner. Thus, you might want to set up separate accounts for each goal, so you can more closely match the investments to your willingness to assume risk for that goal. Please call if you'd like to discuss this concept in more detail. ○○○

Your Plans for Retirement

How much will you need to live a comfortable retirement? It's a question that can't be answered without giving serious thought to how you really want to spend your retirement.

Retirement is no longer viewed as a time to slow down, but is now considered a new beginning in life. Thus, your current living expenses may have little to do with your retirement expenses. However, keep in mind that retirement often proceeds in stages, with different spending trends in each stage. The three basic phases are:

- An active phase, when the retiree is in good health and actively pursues travel and hobbies. This is typically the most expensive retirement phase.
- A passive phase, when the retiree's energy starts to wane. Life starts to slow down, and living expenses typically decrease.
- A final phase, when medical conditions often result in subsistence living. This is typically a more expensive time than the passive



phase due to increased medical expenses, but as long as proper medical arrangements have been made, probably not as expensive as the active phase.

To help you visualize your retirement so you can estimate retirement expenses, consider these questions:

- When do you want to retire? Will you realistically have the resources to retire at that age?
- Do you plan to stay in your current home, trade down to a smaller one, or move to a different city? If you plan to move, is the cost of living more or less expensive than your present city? Have you made extended trips to the new location during different seasons to make sure you'll enjoy living there?
- Will your mortgage be paid off by retirement? What about other debts?
- Will you continue to work after retirement? If so, will you work part-time or full-time? Where will you work, and how much can you expect to earn? Do you have any hobbies or interests that can be turned into paying jobs? Are you planning to start a business after retirement?
- How will you spend your free time? What hobbies will you pursue?

How often and where will you travel? How much will all these activities cost?

- How will you pay for medical costs? Will your employer provide health insurance, or will you need to purchase insurance to supplement Medicare coverage?
- Do you have any medical conditions that are likely to impact your quality of life in retirement? What would you do if you became physically disabled? Would your spouse take care of you, would you move in with your children, or would you go to a nursing home? How will you provide for long-term-care costs?
- How much of your income will be provided by personal investments, including 401(k) investments? Are you confident you can invest so those investments will last your entire retirement? How much of an investment loss could you tolerate without changing your retirement lifestyle?
- What would happen financially if your spouse dies? If you die, would your spouse be able to support himself/herself financially?

If you'd like to review these questions in more detail, please call. ○○○

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Due to lower earnings and more time out of the work force, the average employed woman has a defined-contribution plan balance that is only 60% of the average employed man's balance. Among workers 50 and older, women had saved \$63,000 less than men (Source: LIMRA, 2011).

Approximately 58% of investors with a retirement account or other financial investment reported making at least one change toward being more financially conservative. The top three

Did You Know?

changes reported by investors were increasing savings, shifting away from stocks, and increasing their anticipated retirement age (Source: Investment Company Institute, 2011).

According to a recent survey, 84% of affluent baby boomers expect their retirement to be different from their parents, with most saying they will maintain a more active lifestyle (86%) and enjoy

a higher standard of living (72%). Approximately 70% plan to continue working after reaching retirement age (Source: Bank of America, 2011).

According to a recent study, the majority of working Americans over age 18 will not be able to afford to retire at age 65. At current savings levels, most Americans will need to work until at least age 73 to fund a financially secure retirement (Source: Nyhart, 2010). ○○○